

1 Amend 2 Cal Code Regs. section 18705.1 to read:

2
3 **18705.1. Materiality Standard: Economic Interests in Business Entities.**

4 (a) Introduction.

5 (1) If a business entity in which a public official has an economic interest is
6 directly involved in a governmental decision (see 2 Cal. Code Regs., section 18704.1(a)),
7 use the standards in subdivision (b) of this regulation.

8 (2) If a business entity in which a public official has an economic interest is
9 indirectly involved in a governmental decision (see 2 Cal. Code Regs., section
10 18704.1(b)), use the standards in subdivision (c) of this regulation.

11 (b) Directly involved business entities.

12 (1) General Rule: Unless the exception in subdivision (b)(2) of this regulation
13 applies, the financial effects of a governmental decision on a business entity which is
14 directly involved in the governmental decision is presumed to be material. This
15 presumption may be rebutted by proof that it is not reasonably foreseeable that the
16 governmental decision will have any financial effect on the business entity.

17 (2) Exception: If the public official's only economic interest in the business entity
18 is an investment interest (see Government Code section 87103(a)), and the public
19 official's investment in the business entity is worth \$25,000 or less, then apply the
20 materiality standards in subdivision (c)(1) of this regulation if the business entity is listed
21 on the Fortune 500, or the materiality standards in subdivision (c)(2) of this regulation if
22 the business entity is listed on the New York Stock Exchange, or if not listed on the New
23 York Stock Exchange, ~~for its most recent fiscal year~~ had earnings before taxes of no less
24 than:

1 (A) ~~\$2.5 million, or~~ \$10 in the aggregate for its three most recent fiscal years,
2 together with a minimum of \$2 million for each of its two most recent fiscal years, and
3 positive amounts in all three years, or

4 (B) such other amount described at Rule 102.01C of the New York Stock
5 Exchange's Listed Company Manual (or any superseding rule of the New York Stock
6 Exchange describing its financial standards for initial listing).

7 (c) Indirectly involved business entities. The following materiality standards
8 apply when a business entity in which a public official has an economic interest is
9 indirectly involved in a governmental decision. If more than one of the following
10 subdivisions is applicable to the business entity in question, apply the subdivision with
11 the highest dollar thresholds.

12 (1) If the business entity is listed in the Fortune 500, the financial effect of a
13 governmental decision on the business entity is material if it is reasonably foreseeable
14 that:

15 (A) The governmental decision will result in an increase or decrease in the
16 business entity's gross revenues for a fiscal year of \$10,000,000 or more; or

17 (B) The governmental decision will result in the business entity incurring or
18 avoiding additional expenses or reducing or eliminating existing expenses for a fiscal
19 year in the amount of \$2,500,000 or more; or

20 (C) The governmental decision will result in an increase or decrease in the value
21 of the business entity's assets or liabilities of \$10,000,000 or more.

22 (2) If the business entity is listed on the New York Stock Exchange, or if not
23 listed on the New York Stock Exchange, ~~for its most recent fiscal year~~ had earnings

1 before taxes of no less than ~~\$2.5 million~~ \$10 in the aggregate for its three most recent
2 fiscal years, together with a minimum of \$2 million for each of its two most recent fiscal
3 years, and positive amounts in all three years, or such other amount described at Rule
4 102.01C of the New York Stock Exchange's Listed Company Manual (or any
5 superseding rule of the New York Stock Exchange describing its financial standards for
6 initial listing), the financial effect of a governmental decision on the business entity is
7 material if it is reasonably foreseeable that:

8 (A) The governmental decision will result in an increase or decrease to the
9 business entity's gross revenues for a fiscal year in the amount of \$500,000 or more; or,

10 (B) The governmental decision will result in the business entity incurring or
11 avoiding additional expenses or reducing or eliminating existing expenses for a fiscal
12 year in the amount of \$200,000 or more; or,

13 (C) The governmental decision will result in an increase or decrease in the value
14 of assets or liabilities of \$500,000 or more.

15 (3) If the business entity is listed on either the NASDAQ or American Stock
16 Exchange, or if not so listed, for its most recent fiscal year had: net income of no less
17 than \$500,000 (or such other amount described in the minimum financial requirements
18 for continued listing on the NASDAQ ~~SmallCap market~~ Capital Market), or earnings
19 before taxes of no less than \$750,000 (or such other amount of earnings before taxes
20 described under initial listing standard 1 of Section 101(a) of the Rules of the American
21 Stock Exchange, or any superseding Section of the Rules of that Exchange), the financial
22 effect of a governmental decision on the business entity is material if it is reasonably
23 foreseeable that:

1 (A) The governmental decision will result in an increase or decrease to the
2 business entity's gross revenues for a fiscal year in the amount of \$300,000 or more; or,

3 (B) The governmental decision will result in the business entity incurring or
4 avoiding additional expenses or reducing or eliminating existing expenses for a fiscal
5 year in the amount of \$100,000 or more; or,

6 (C) The governmental decision will result in an increase or decrease in the value
7 of assets or liabilities of \$300,000 or more.

8 (4) If the business entity is not covered by subdivisions (c)(1)-(3), the financial
9 effect of a governmental decision on the business entity is material if it is reasonably
10 foreseeable that:

11 (A) The governmental decision will result in an increase or decrease in the
12 business entity's gross revenues for a fiscal year in the amount of \$20,000 or more; or,

13 (B) The governmental decision will result in the business entity incurring or
14 avoiding additional expenses or reducing or eliminating existing expenses for a fiscal
15 year in the amount of \$5,000 or more; or,

16 (C) The governmental decision will result in an increase or decrease in the value
17 of the business entity's assets or liabilities of \$20,000 or more.

18 (d) Terminology. The accounting terms described below are the same as, or not
19 inconsistent with, terms used in Generally Accepted Accounting Principles and Generally
20 Accepted Auditing Standards. Nothing in this subdivision should be construed to
21 incorporate new items not contemplated under Generally Accepted Accounting Principles
22 and Generally Accepted Auditing Standards, nor to exclude any items that might be

1 included in the definitions of these terms under Generally Accepted Accounting
2 Principles and Generally Accepted Auditing Standards.

3 (1) Assets. As used in this section, "assets" means all property, real and personal,
4 tangible and intangible, which belongs to any business entity. This includes, but is not
5 limited to, cash, securities, merchandise, raw materials, finished goods, operating
6 supplies, and ordinary maintenance material and parts, accounts receivable and notes and
7 loans receivable, and prepaid expenses (such as prepaid insurance, interests, rents, taxes,
8 advertising, and operating supplies).

9 (A) When a business entity holds a claim over collateral (including real property)
10 as security for a loan made by the business entity, such a claim does not make the
11 collateral (including real property) an "asset" of the business entity, unless the business
12 entity has initiated proceedings to foreclose upon, or acquire the asset based on the
13 debtor's failure to repay the loan. The loan or note secured by the collateral is an asset.

14 (B) The definition of "assets" also includes intangible assets. Intangible assets,
15 include, but are not limited to, long-lived legal rights and competitive advantages
16 developed or acquired by a business enterprise, patents, copyrights, franchises,
17 trademarks, organizational costs, goodwill, and secret processes.

18 (2) Earnings Before Taxes: Revenue, less the cost of goods sold and selling,
19 general, and administrative expenses (but not excluding depreciation and amortization
20 expenses); otherwise defined as operating and non-operating profit before the deduction
21 of income taxes. Described variously as EBT, Income Before Income Taxes, or Income
22 Before Provision for Income Taxes.

1 (3) Expenses: In general, the term refers to the current costs of carrying on an
2 activity.

3 (4) Gross Revenue: Actual or expected inflows of cash or other assets. "Gross
4 Revenue" is the revenue of a business entity before adjustments or deductions are made
5 for returns and allowances and the costs of goods sold, and prior to any deduction for
6 these and any other expenses.

7 (5) Liabilities: Obligations of the business entity, liquidation of which is
8 reasonably expected to require the transfer of assets or the creation of other new
9 liabilities. Any financial obligation or cash expenditures that must be made by the
10 business entity at a specific time to satisfy the contractual terms of such an obligation.

11 (6) Net Income: A business entity's total earnings; otherwise defined as revenues
12 adjusted for the costs of doing business, depreciation, interest, taxes, and other expenses.
13 This amount is usually found at the bottom of a business entity's Profit and Loss
14 statement. Also described as Net Profit.

15 (e) Financial statements. In complying with this regulation, public officials may
16 rely on the most recent independently audited financial statements of the business entity
17 so long as those statements are reflective of the current condition of the business entity.
18 Financial statements are not considered "reflective of the current condition of the
19 business entity" where:

20 (1) The most recent independently audited financial statements of the business
21 entity are for a fiscal year ending more than twenty-four months prior to the date of the
22 governmental decision.

1 (2) The most recent audit of the financial statements resulted in an adverse
2 opinion, was issued with a disclaimer, or was otherwise qualified in such a manner that
3 the statement of assets, liabilities, expenses, or gross revenues is questioned in the audit
4 report, or

5 (3) There has been a subsequent event, intervening between the date that the
6 financial statement was created and the date of the decision of the public official, that
7 makes the statement no longer representative, including, but not limited to, business
8 reorganizations.

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10 NOTE: Authority cited: Section 83112, Government Code.

11 Reference: Sections 87100, 87102.5, 87102.6, 87102.8 and 87103, Government Code.

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13 COMMENTS: Electronic access to annual reports, quarterly reports, and other financial
14 statements filed with the United States Securities and Exchange Commission (“SEC”)
15 may be obtained by accessing the SEC’s website and selecting its EDGAR database of
16 statutory filings: <http://www.sec.gov/edgar/searchedgar/companysearch.html>.

17 The earnings before taxes and net income criteria for listing on the New York and
18 American Stock Exchanges, and NASDAQ may be obtained through links from the
19 following webpages:

20 New York Stock Exchange: <http://www.nyse.com/listed/listed.html>.

21 American Stock Exchange: <http://wallstreet.cch.com/AmericanStockExchangeAMEX/>.

22 NASDAQ: http://www.nasdaq.com/about/nasdaq_listing_req_fees.pdf.